Saving Money on Retiree Health Insurance

Municipalities have experienced tremendous fiscal stress due to the dramatic increases in employee health care costs. In many ways, communities have little control over these costs given the difficulty with bargaining changes for all unions before implementing higher employee contributions. Nonetheless, some communities such as the City of Springfield have opted to accept Section 18 of MGL Chapter 32B in order to save money on retiree health insurance. In its simplest terms, this section allows a community to shift a significant portion of its retiree health care costs to the federal Medicare program. For Springfield, these cost savings are projected to total almost $19 million dollars over the next three years.

Section 18 of Chapter 32B can be adopted by majority vote of the city council in a city with a Plan D or Plan E charter, or by the council, with the approval of the mayor, in any other city. In towns, acceptance by either a majority vote of town meeting or the electorate is required. Once adopted, Section 18 requires that all eligible retirees enroll in Medicare Part B. Though not all will be eligible, retirees may be eligible if they paid into the Medicare system for at least 10 years during their local government employment, during prior employment, or if a spouse contributed to Medicare. Those that are eligible likely have been automatically enrolled in Medicare Part A.

Municipal cost savings arise when retirees enroll in Medicare as this federal insurance program covers a substantial portion of their health costs. For example, Medicare Part A covers inpatient care in hospitals including critical access hospitals or skilled nursing facilities when medically necessary. Medicare Part B covers up to 80 percent of doctors' services and outpatient care. Together, the two Medicare plans provide a significant level of health coverage, however, deductibles and co-payments to the retiree are often high.

To protect the retiree from these additional costs, Section 18 also requires retirees to enroll in a Medicare extension plan that covers any gaps in the coverage provided by Medicare. The purpose of mandating enrollment in an extension plan is to ensure that retirees do not receive any lesser coverage than they received prior to the adoption of Section 18. In fact, Section 18 states explicitly that the actuarial value of the coverage under the Section 18 plans must be comparable to the retiree's existing coverage.

Extension plans are offered by private insurers to municipalities on a group basis to supplement Medicare coverage. Costs for these plans are generally significantly lower than they are for regular, full-featured municipal health insurance plans due to the fact that they need only supplement the federal Medicare coverage. Since the extension plan insurance is much cheaper than the regular municipal insurance, savings arise. How these savings are allocated between the municipality and the retirees depends on the municipal contribution to regular retiree health plans, the contribution toward the supplemental plans and whether there is any municipal subsidy to help the retiree pay the Medicare B premiums. The retiree's savings may be enough to cover the monthly premium the retiree must now pay to enroll in Medicare. For retirees that were paying both Medicare and regular health premiums, savings that arise due to the substitution of a less expensive extension plan will be a windfall.

While the municipality saves money based on its share of the reduced costs to provide the extension plan, there are premium penalties for late enrollment in Medicare. By law, however, these penalties must be paid by the municipality rather than the retirees. The penalties are calculated based on the period that a retiree was eligible, but not enrolled in Medicare. For example, the initial enrollment period for Medicare B is a seven-month period that extends from the three-month period preceding the month the employee turns age 65 through the three-month period following this month. For each full year that an employee was eligible, but not enrolled, a penalty of 10 percent of the Medicare B premium ($78.20 per month in 2005) is assessed.

Projecting the saving to a municipality is somewhat complex and depends on the share of health costs covered, the cost difference between the regular municipal plans and the extension plans, and the premium penalties assessed. Springfield hired a consultant to assist the city in projecting the expected cost savings and penalties. This analysis entailed reviewing past claims to determine which costs Medicare would have covered and reviewing retirees' ages to calculate premium penalties. Another factor in any analysis will be the impact of Medicare prescription drug coverage (Medicare Plan D) that became available on January 1, 2006. Communities that choose to continue to provide drug coverage to their retirees will be eligible for a reimbursement from Medicare for a portion of their retirees' drugs costs.

A significant consideration when adopting Section 18 is to understand the collective bargaining implications. Based on a recent complaint issued by the Massachusetts Labor Relations Commission (MLRC), an employer's bargaining obligation regarding the implementation of Section 18 is limited to currently active employees and does not extend to retirees. In its decision, the MLRC stated "a public employer need not bargain with the union representing active employees prior to changing health insurance terms, costs and benefits for employees who have already retired". However, the Commission did find that the future retirement benefits of active workers are part of their overall compensation and that, as such, changes to those benefits must be impact bargained (See Chemical Workers v. Pittsburgh Plate Glass Co., 404 U.S. 157 (1971)). As this is a very specialized area of the law, we suggest that labor counsel be consulted prior to moving forward.

Another factor when adopting Section 18 is the commitment required to provide explanatory sessions for retirees and public officials. Springfield conducted approximately two-dozen sessions, however, the concurrent switch in health carriers may have complicated their experience. Nevertheless, it is important that all involved understand that despite some of the complicated details, the level of retiree health coverage will not change, merely who pays for it.

(Marilyn Montagna, Personnel Director of the City of Springfield, contributed to this article.)